

CALIFORNIA ENERGY COMMISSION

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May 19, 2005

Mr. James P. Mayer
Executive Director
State of California Little Hoover Commission
925 L Street, Suite 805
Sacramento, CA 95814

Dear Mr. Mayer:

I am responding to the letter you sent to my office on May 16, 2005. Enclosed you will find a copy of the written testimony I will be giving before the Little Hoover Commission on May 25, 2005.

I have based my testimony on the questions you have asked: 1) What are the greatest energy problems facing California and what is the Schwarzenegger Administration's strategy for responding to these challenges?; 2) How does the State's organizational structure contribute to these problems or impede the resolution of these problems? How does the reorganization plan resolve these deficiencies?; 3) What is the administration expecting to accomplish with its energy policy and how will it measure progress toward those goals: How will the reorganization plan contribute to that progress? How will you implement and monitor the new structure to maximize its role in developing an effective energy policy?

If you should need additional information, please contact me at (916) 654-5000.

Sincerely,

A handwritten signature in blue ink that reads "Joseph Desmond".

JOSEPH DESMOND
Chairman

Enclosure

Testimony of Joseph Desmond
Chairman, California Energy Commission

Hearing on the Governor's Reorganization Plan to Create a Department of Energy
Little Hoover Commission
May 25, 2005

Thank you, Commissioners, for the opportunity to discuss the Governor's Energy Reorganization Plan – A Vision for California's Energy Future. As the new Chairman of the California Energy Commission and the Governor's Energy Advisor, it is my pleasure to provide you with an overview of the Governor's plan to improve the effectiveness of developing and implementing energy policy in California.

You have asked us to respond to the following three questions.

1. What are the greatest energy problems facing California and what is the Schwarzenegger Administration's strategy for responding to these challenges?
2. How does the State's organizational structure contribute to these problems or impede the resolution of these problems? How does the reorganization plan resolve these deficiencies?
3. What is the Administration expecting to accomplish with its energy policy and how will it measure progress toward those goals? How will the reorganization plan contribute to that progress? How will you implement and monitor the new structure to maximize its role in developing an effective energy policy?

I will address these questions within these formal comments.

Energy Reorganization – An Idea Who's Time Has Come (Again)

The concept of reorganizing and consolidating energy agencies is not new to state government. As early as 1984, the Little Hoover Commission found that the Energy Commission lacked an effective mechanism to put its policy recommendations into action, noting the overlap and duplication between the Energy Commission and the California Public Utilities Commission (CPUC).ⁱ In responding to a reorganization proposal submitted by the Wilson Administration in 1995, the Little Hoover Commission declared that reorganization represents "an important opportunity to align similar functions so that increased efficiency, effectiveness, and accountability are achieved."ⁱⁱ Similar observations have been made by the state Legislature in 1989 and 1990, the Legislative Analyst's Office in 2002, and the Public Policy Institute in 2003.

The implementation of Assembly Bill 1890 and the Electricity Crisis of 2001 added to the problem. California has even more energy boards, authorities and offices addressing energy issues than it did prior to restructuring.

State agencies have taken some steps to more efficiently address the myriad of energy issues requiring coordination. In 1999, the Energy Commission and the CPUC began collaborating on electricity and natural gas issues. Since 2003, several state agencies with various energy

responsibilities have participated in an Energy Action Plan working group, providing a principal venue to address several of the more complex electricity issues, energy agency responsibilities, and direction for California's energy policies. In 2002, passage of Senate Bill 1389, formalized an approach for integrated energy policy, the Energy Commission leading that effort. However, more work remains to be done.

Addressing California's Energy Challenges

As important as avoiding another crisis is, energy policy must go beyond this and support fundamental economic, environmental and risk management policy goals that promote the financial well-being of Californians, improve the health of our economy in the short term, and return California to its leadership position in the longer term. Policies must preserve and protect California's environment, one of our state's great assets.

Your letter asked "What are the greatest energy problems facing California and what is the Schwarzenegger Administration's strategy for responding to these challenges?"

Many of the energy challenges facing California today have been identified in the Governor's electricity plan and outlined his upcoming response to the 2003 and 2004 Integrated Energy Policy Report that is being prepared for the Legislature. To summarize the challenges facing California, we must:

- ensure adequate, reliable and affordable energy resources including natural gas, renewable energy; and transportation fuels;
- insure competitive wholesale electricity procurement;
- invest in energy infrastructure that relieves transmission congestion and improves the movement of generation throughout the state (i.e., bulk transmission lines);
- reduce electricity and natural gas rates and decrease price volatility;
- pursue refunds from Federal Energy Regulatory Commission (FERC) for generator overcharges;
- continue renegotiating many of the Department of Water Resources power contracts;
- reduce dependency on petroleum.

This proposal optimizes the ability of state policymakers to respond to these challenges. It builds on the functional relationships and responsibilities of the Energy Action Plan, and the Integrated Energy Policy Report process. It considers the recommendations and responses of the California Performance Review, as well as input from many others from government, industry and representative consumer and environmental groups. It seeks to institutionalize the interagency collaborations through the creation of a Department of Energy, with a Cabinet-level Secretary that will consolidate fragmented energy functions and authorities, reduce overlap by multiple state agencies and make government more responsive to its citizens.

Key Focus: Accountability

The new department will assume responsibility for several energy programmatic functions now being performed by the Energy Commission. The staff and functions of several departments, commissions and offices will be consolidated under the direction of the new department. This reorganization improves accountability, focuses the development of energy policy, reduces

fragmentation and duplication, and improves communications with the Legislature, the public, the Administration, and the federal government.

With the establishment of a Department of Energy, clear energy policy and a clearly-defined policy authority will exist. By comparison, today's environment presents inconsistencies about which agency speaks for California in the area of energy policy.

Consolidate and Increase Effectiveness

Under this plan, the current California Energy Commission and the Electricity Oversight Board will be housed within the proposed Department of Energy structure. The newly structured Energy Commission, comprised of four commissioners and chaired by the new Energy Secretary, will continue to license power plants 50 megawatts or larger, and to develop and approve energy building and appliance efficiency standards. Additionally, the Energy Commission will be given expanded licensing authority over new natural gas pipeline proposals, natural gas storage facilities and 200kV transmission lines that are operated by the Independent System Operator. Smaller transmission projects between 50kV and 200kV will be processed through an expedited Energy Commission process modeled after the current process used by the CPUC. Recognizing the serious challenges facing the State as it attempts to ensure a reliable electricity grid, the new process allows for streamlined transmission line permitting that can be integrated with power plant licensing.

Transmission and natural gas pipeline and storage licensing responsibilities -- now within the CPUC -- will be transferred to the newly structured Energy Commission. The proposal also moves the administration of the State's natural gas and electricity contracts -- now managed by the California Energy Resources Scheduling from the Department of Water Resources -- to the new department, along with the financing authority from the now unfunded California Consumer Power and Conservation Authority (CPA).

The Electricity Oversight Board's existing market oversight functions will be transferred to the Office of Energy Market Oversight within the Department of Energy. Among its other responsibilities and consistent with its current regulatory authority, the Office of Energy Market Oversight will continue to represent the interests of California's consumers before the FERC.

Regarding your third question, measuring progress toward the implementation of state energy policy is a key component of the current IEPR process and will continue to be under the new organizational structure. The present "progress-to-plan" approach was established by the Energy Commission in 2004, whereby energy policies adopted by the Administration are tracked to determine how effectively the state agencies are implementing these policies. In today's structure, no entity or individual is held accountable if progress falls short of expectations. Under the proposed department structure, the Secretary of Energy will be held accountable for progress.

The proposal for a new Department of Energy is a culmination of the efforts of the California Performance Review and its public proceedings incorporates recommendations contained in various reports authored by the Bay Area's Economic Forum, the California Attorney General, the Legislative Analyst's Office and the Energy Commission's 2003 and 2004 Integrated Energy Policy Report to the Governor and the Legislature. The proposal preserves what the current Energy Commission has done so well for over 30 years and builds on an existing core of a knowledgeable and trained staff and successful programs.

While this reorganization plan suggests several changes to the structure of the state's energy agencies, it is important to note that this proposal does not change the California Environmental Quality Act or the state's ability to effectively respond to the Act's provisions. With respect to the CPUC, the proposal does not alter its critical ratemaking responsibilities and other related functions. The proposed reorganization also does not inhibit the statutory and regulatory responsibilities of the other boards and commissions.

To summarize, in this reorganization of energy agencies and their functions, the Administration's authority for energy policy is vested with a California Secretary of Energy, empowered to make decisions regarding energy policy. This creates an identified center of accountability, insuring that that California sends clear and consistent energy messages to the public, the business community, the energy industry and financial markets. The California Department of Energy, headed by the Secretary of Energy, consolidates the state's considerable technical energy expertise, develops and implements energy policies and programs, and continues providing technical support for licensing power plants and establishing building and appliance efficiency standards. The newly-proposed Energy Commission's focus on licensing generation facilities and adopting energy efficiency standards for buildings and appliances -- plus an expanded energy facilities licensing authority for transmission lines and natural gas pipelines and storage facilities -- will maintain the public's crucial involvement in energy infrastructure decisions, as well as, the Commission's independence in those licensing energy facilities.

Thank you for giving me this opportunity to testify before you today.

ⁱ *A Study of the Organization and Coordination of Electric Energy Planning and Electric Utility Regulation in California*, Little Hoover Commission, February 1984. *Senate Concurrent Resolution 7*, 1989. *Legislature's Joint Committee on Energy Regulation and the Environment*, February 1991. *Review of the Governor's Reorganization Plan No 1*, Little Hoover Commission, March 1995.

ⁱⁱ *Review of Governor's Reorganization Plan #1*, Little Hoover Commission, March 1995.